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IN THE

Supreme Court of the United States.

OCTOBER TERM, 1932.

No. 8.

NATIONAL SURETY COMPANY, *et al.*,
Petitioners (Appellants Below),

vs.

VALERIA E. CORIELL,
Respondent (Appellee Below),

MORRIS WHITE, INC.,
Respondent (Appellee Below),

IRVING TRUST COMPANY, as Receiver of Morris White, Inc.,
Respondent (Appellee Below),

MICHAEL HOLLANDER, *et al.*, constituting a Committee of Creditors of Morris, White, Inc.,
Respondent (Appellee Below).

BRIEF FOR RESPONDENTS ON WRIT OF CERTIORARI TO REVIEW ORDER OF THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, DATED NOVEMBER 25, 1931.

JOSEPH GLASS,
JOHN S. SHEPPARD,
JEROME WEINSTEIN,
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Counsel for Respondents.

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(Appellee Below).

BRIEF FOR RESPONDENTS

The Writ Herein and the Questions Raised Thereby.

This case comes before the Court upon a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit, issued on May 16, 1932 (286 U. S. 537).

That writ was granted on a petition for certiorari filed herein on February 23, 1932 (October Term, 1931—No. 727) (R. 175). In said petition (p. 2) petitioners sought review of the decree of the United States Circuit Court of Appeals for the Second Circuit, entered on November 25, 1931, modifying a decree made by Judge KNOX of the United States District Court for the Southern District of New York, dated June 15, 1931. That decree of the District Court authorized Irving Trust Company, as receiver, to accept the offer, made pursuant to a plan of reorganization, for the purchase of the assets of the defendant. That offer provides, in substance, that the creditors of Morris White, Inc. be paid 100% of their allowed claims in the following manner: 20% in the notes and 80% in the preferred stock of the reorganized corporation R. 165, 166). Upon the petitioners' appeal to the Circuit Court of Appeals, that Court held that petitioners had a right to be paid in cash their proportionate share of the price which would have been realized on a public sale of the assets after deduction of administration expenses (R. 173).

The Circuit Court directed, in substance, that a Special Master ascertain the value of the defendant's assets as if sold for cash at a public sale on June 15, 1931, and that, out of the sum so ascertained, petitioners be awarded their ratable shares, to be paid to them in cash (R. 173, 174). It further directed that, at petitioners' option, "the preferred stock and notes offered to them may be valued as of the date the reorganization became effective, and that sum paid in cash to them or either of them" (R. 174).

The petition for certiorari granted herein (October Term, 1931—No. 727) recites (pp. 6, 7):

"THE QUESTIONS PRESENTED.

1. Did the Circuit Court of Appeals rightly decide that the petitioners' right was merely to an aliquot share in cash of such sum as a Special Master may find would have been realized if the property of Morris White, Inc. had been sold at public sale on June 15, 1931?

2. Or should the Circuit Court of Appeals have reversed entirely the decree of the District Court dated June 15, 1931, and have directed that the property of the defendant be sold?

3. Did the Circuit Court of Appeals rightly decide that the rights of these petitioners could be fully protected by relegating them, months after the actual transfer had occurred, to a mere guess of a Special Master as to what might have been realized at a public sale six or more months previously, which sale was never held and the terms and methods of which were never determined?

4. If the Circuit Court of Appeals was otherwise right, did it rightly limit the security of the petitioners for the payment of their aliquot share in cash to what might be collected by a sale of the property of Morris White, Inc. transferred to the new corporation, notwithstanding that in the interval much of that property would inevitably be consumed in the new corporation's business before such a sale could be made?"

This Court has repeatedly ruled that it will limit its review on certiorari to the questions raised in the petition upon which the writ was granted.

Steele v. *Drummond* (1927), 275 U. S. 199, 203;
Commercial Credit Co. v. *United States* (1928), 276 U. S. 226, 230;
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* * * * * * * *

A considerable part of petitioners' brief (pp. 39, *et seq.*) is devoted to an attack upon the administration of this estate

in an equity receivership rather than in bankruptcy proceedings. Petitioners argue that such administration deprived them of their rights under the Bankruptcy Act. Those arguments have already twice been considered and twice overruled by this Court in the instant case.

Simultaneously with the filing of the petition granted herein, these petitioners filed a separate petition for a further writ of certiorari herein (October Term, 1931—No. 726). In said petition, petitioners sought review of the order of the United States Circuit Court of Appeals for the Second Circuit entered on November 25, 1931, which affirmed an order of the United States District Court for the Southern District of New York, dated June 3, 1931, appointing Irving Trust Company as permanent receiver in equity of the defendant, Morris White, Inc. In said petition (pp. 2, 3, 7) petitioners attacked the appointment of a permanent receiver in equity upon the ground that the estate of the defendant, Morris White, Inc., should have been administered in bankruptcy and that administration in equity deprived petitioners of their rights and remedies under the provisions of the Bankruptcy Act. *That petition was denied* by this Court on May 16, 1932 (286 U. S. 553). Thereafter, petitioners applied for rehearing on said petition. *Rehearing was denied* by order of this Court entered October 10, 1932. We believe that this Court, in denying that petition, has given full and careful consideration to petitioners' arguments with respect to the propriety of administration of the estate in equity rather than in bankruptcy.

This brief will, therefore, be confined to the questions raised in the petition which has been granted.

We deem it necessary, however, to refer briefly to petitioners' attack upon the appointment of complainant's solicitors as counsel for the receiver. The fact that the bill of complaint herein had been filed by the receiver's counsel is openly disclosed by the record (R. 7). It was fully known to the District Court. The selection by that Court of a firm of counsel, known to it to be counsel for the complainant, as counsel also for the receiver, was a matter within the discre-

tion of that Court. Such appointment was the act of the Court and violated no rule or order of the Court. It denoted the confidence of Judge KNOX in such counsel. After an open disclosure of the fact that such firm represented complainant, the Court deemed it to be in the best interests of the estate that they be selected as counsel for the receiver and entered an order so appointing them. That order has never been attacked and is no part of the present record. No assignment of error on the appeal to the Circuit Court was predicated on such appointment (R. 160-163). No such objection was made before the District Court. *No such objection appears anywhere in the record.* It has no proper place before this Court.

If petitioners deem such appointment improper, they may still assert their objections in proper and orderly fashion at the time that receiver's counsel make application for allowance. No allowance has as yet been made and all allowances still remain "subject to the approval" of the District Court (R. 152), although petitioners' brief may create a different impression.

While, therefore, receiver's counsel are sensitive to the implications suggested in petitioners' attack upon their appointment, and are prepared to argue that matter *in extenso* before any proper forum, they do not feel that any further statement need be made before this Court, in view of the clear irrelevance of the matter here.

The inferences of fact appearing in petitioners' brief are somewhat misleading. We deem it essential to furnish our own statement of the facts relevant to the questions presented on the writ granted herein.

Statement of Facts.

The Nature and History of Defendant's Business.

The defendant corporation, a New York corporation, was engaged in the manufacture and sale of ladies' handbags and fancy leather goods (R. 1, 68). In this industry, it was the

largest concern in the world (R. 68). It employed between three and four thousand people (R. 68).

Until the recent depression, it had a consistent record of profits (R. 90). In 1925 it did a business of $5,807,000 and its profits were $400,000 (R. 90). In 1926, it did a business of more than $7,000,000 and its profits were in excess of $700,000 (R. 90). In 1927, it did a business of $7,600,000 and its profits were $556,000 (R. 90). In 1928, it did a business of $8,546,000 and its profits were $716,000 (R. 90). In 1929, it did a business of $6,890,000 and its profits were $600,000 (R. 90).

When the present depression began, defendant had on hand orders for $2,000,000 from stores like Marshall Field & Co., Carson, Pirie & Scott, and similar concerns (R. 74). Of such orders $1,500,000 were cancelled (R. 74). In the nature of defendant's business it was required to carry large inventories of raw materials—leather, silks, frames, ornaments, etc. (R. 62). The trend of prices for the past three years is a matter of which this Court has taken judicial notice.

Less than a year prior to the appointment of the receiver, the defendant owed more than $3,000,000 to its creditors (R. 74). That indebtedness had been reduced to $1,072,000 at the date of appointment of the temporary receiver (R. 135).

During the five months preceding the appointment of the temporary receiver, the defendant had been operating its business under the control of creditors (R. 74). Two creditors refused to cooperate with the other creditors (R. 2). Pfister & Vogel Leather Company, on or about April 1, 1931, obtained a judgment against the defendant in the sum of approximately $25,000 (R. 2, 35) and caused execution to be levied (R. 2, 35).

The Appointment of a Receiver.

Following such levy, the complainant, Valeria E. Coriell, a creditor for $27,900, (R. 4) filed a general creditors' bill for the appointment of a receiver to administer defendant's

assets (R. 1-7). The complainant was the assignee of The New Jersey National Bank & Trust Company, a resident of the State of New Jersey (R. 4). The indebtedness alleged was a balance due upon a promissory note (R. 4). The defendant answered and consented to the appointment of a receiver (R. 7, 8).

On April 6, 1931 Irving Trust Company was appointed temporary receiver (R. 8-15). Thereafter, the receiver gave due notice to all creditors of a hearing on the matter of making the receivership permanent (R. 142). After such hearing, and on June 3, 1931, an order was entered making the receivership permanent (R. 141).

The Creditors' Committee.

On call of the receiver, a meeting of creditors was held on April 14, 1931 (R. 17, 56, 72). Creditors with claims in the total amount of $747,000, as ascertained by a poll of those present, attended that meeting (R. 17, 72). The receiver made a preliminary report on the general status of the defendant's business (R. 17, 56). A statement of the assets and liabilities of the defendant as of April 6, 1931, prepared by Kline, Hinds and Finke, certified public accountants, *selected by the creditors,* was read (R. 56, 75, 134-5). The receiver expressed its views as to the value of the assets listed therein (*id.*).

A Creditors' Committee was formed at that meeting (R. 17, 56). That Committee was elected by the unanimous vote of all creditors present (R. 17, 72). It consisted of nine members (R. 17, 32). That Committee included Mr. Hollander, representing a bank creditor (R. 56), Mr. Jephson, representing the Textile Banking Corporation, commercial factors, a merchandise creditor for $40,000 (R. 56), Mr. Weisman, representing the bank creditors; Mr. Rosenberg, representing the Rex Novelty Works, a merchandise creditor for $32,000 (R. 17, 56, 62); Mr. Quigan, a merchandise creditor for $14,000 (R. 56); Mr. Schoenfeld, representing Ar-

tistic Wire Forming Corporation, a merchandise creditor for $30,500 (R. 56); Mr. Hausman, a merchandise creditor for $20,000 (R. 56); and Mr. Bernheim, a merchandise creditor for the sum of $42,000 (R. 62). The Committee directly represented merchandise creditors with claims of approximately $178,000, and the five bank creditors to whom there was owing $262,500 upon unsecured claims and $179,000 upon secured claims (R. 72). The total amount of claims directly represented by the Committee was approximately $600,000.

At the suggestion of that Committee, Mr. Moakes, the representative of the National Surety Company—the leading petitioner—became a member of the Committee *ex-officio* (R. 72, 73). Mr. Moakes participated in all the deliberations of that Committee (R. 72, 73, 124) and himself stated at the hearing before Judge KNOX: "It is true I attended every meeting" (R. 124). Mr. Moakes further stated that he had submitted to the National Surety Company the Committee's various reports (R. 124). The following also appears in the record (R. 124):

> "Mr. Stern: Mr. Moakes, isn't it a fact that you had the full accountant's report of Kline, Hinds & Finke, a photostatic copy of the full report, comprising many many pages?
> Mr. Moakes: That is right."

To the leading petitioner at least, the Creditors' Committee fully disclosed its activities.

The Liabilities of Defendant.

The statement of assets and liabilities of the defendant Morris White, Inc. as of April 6, 1931, prepared by Kline, Hinds & Finke, certified public accountants selected by the creditors, reflects liabilities in the sum of $1,072,000.30 (R. 134-5). $441,616.81 was due to banks (*id.*) and $397,045.12 was due to merchandise creditors (*id.*). Mer-

chandise creditors numbered approximately two hundred forty-five (R. 91). There were five bank creditors (R. 69).

Other substantial items of liability listed in the accountants' statement were $80,624.36 due to the Government of the United States for taxes, $57,697.69 due to the State of New York for taxes, and $16,388.04 for the accrued payroll of defendant's employees (R. 134-5). The Government of the United States had filed its claim with the receiver for $100,000 (R. 50). The State of New York had filed a claim for $57,000 (*id.*). These amounts included taxes, interest and penalties (*id.*). These claims were preferred claims. They were entitled to priority.

Regardless of whether the estate were liquidated in bankruptcy or in equity, the expense of administration would have been substantial. Thus it appears that, on the date of the appointment of the receiver herein, there were preferred charges against the estate for approximately $200,000, to be satisfied prior to distribution to general creditors.

The Nature and Value of Defendant's Assets.

The same accountants' statement (R. 125) lists total assets of $4,116,251.04 (R. 134-5) The statement shows current assets of $1,552,740.34 (*id.*). The largest current asset is represented by merchandise inventories listed at $1,241,208.09 (*id.*). Other current assets listed include in approximate amounts, $5,000 in cash, $300,000 in accounts receivable and $4,000 in listed securities. Approximately $250,000 of the accounts receivable had been pledged as collateral to banks for loans *concurrently* made (R. 134, 72).

The Creditors' Committee elected at the meeting of creditors held on April 14, 1931, appointed a sub-committee to determine the realizable value of the assets (R. 61). That sub-committee met and appraised the estate (R. 61). On that sub-committee were Mr. Hausman, in the cotton and rayon business, Mr. Quigan, in the leather business, Mr. Bernheim, in the leather business, Mr. Rosenberg, in the ornament busi-

ness, and Mr. Schoenfeld, in the wire frame business (R. 61-2).

These men were the creditors who had sold the substantial part of the inventory to the defendant (R. 62). They were all unsecured creditors (R. 62). Their claims averaged in excess of $25,000 each (R. 61, 62).

The Committee reported that the merchandise inventory, listed in the accountants' statement at $1,249,000, was worth $717,000 on a going concern basis and $357,000 on a forced sale in liquidation (R. 62). Finished merchandise listed in the accountants' statement at $508,000 (R. 134) was estimated to have a value of $325,000 on a going concern basis and a value of $207,000 upon forced sale (R. 62). The unfinished merchandise showed far greater shrinkage. Leathers listed in the accountants' statement at $316,000 were appraised by leather merchants on the committee to have a value of $255,000 on a going concern basis, and a value of $75,000 upon a forced sale (R. 62). Frames for handbags listed in the accountants' statement at $161,000 were valued at $80,000 on a going concern basis and at $25,000 upon forced sale in liquidation (R. 62). The Committee's figures indicated that a going concern would realize over $350,000 more upon the current inventory than could be realized on a forced sale in liquidation. Among the other assets of the defendant were machinery and equipment. The machinery and equipment of the defendant were valued at $200,000 on a going concern basis (R. 118). That machinery and equipment, it was estimated, would realize $10,000 if sold at auction (R. 118, 119).

One of the other assets listed in the accountants' statement was a note of the Morris White Holding Company to the defendant Morris White, Inc., in the sum of $1,700,000. This represented moneys loaned (R. 78). The Holding Company owned a number of valuable parcels of real estate in the City of New York, including the Fifth Avenue Hotel, the Hotel White and the Whitehall Hotel (R. 78). In April, 1930, the Morris White Holding Company had raised two

and a quarter million dollars upon its properties by a loan from S. W. Straus & Co. (R. 122). These moneys were turned over to the defendant Morris White, Inc. and used to pay creditors of Morris White, Inc. (R. 122). The Holding Company was threatened with the foreclosure of a blanket second mortgage and unsecured creditors of that company had filed a petition in bankruptcy against it. There was no likelihood of any immediate realization on that asset (R. 78).

On a forced sale, there would have been sacrificed an inventory worth $717,000 on the basis of a going concern, machinery and equipment worth $200,000 to a going concern, and the largest item of all—the good will inherent in a business which was the largest in its industry and which theretofore had consistently done an average annual business in excess of $5,000,000 and had consistently earned annual profits averaging in excess of $500,000 a year.

The Plan of Reorganization.

After appraising the assets, the Creditors' Committee drafted a plan of reorganization (R. 73, 74). That plan is embodied in the offer of Lily White, dated April 29, 1931 (R. 17). The plan was unanimously approved by the Creditors' Committee (R. 17). It was then submitted for approval to the District Court and to all creditors (R. 15-34).

The terms of the offer, as submitted to the Court, were modified pursuant to the directions of Judge KNOX made upon the hearing (R. 152, 153). The offer as finally approved by the Court (R. 18-32, 151-155) provides for the transfer of all of the defendant's assets, less the amount required to satisfy the obligations of the receiver and the fees and expenses of administration, to a corporation to be organized. This corporation is referred to as the New Corporation (R. 20). The fees and allowances of the receiver and the receiver's counsel and all other allowances for services rendered in the proceeding or incident to the said offer and its acceptance, payable out of the assets of the estate, are expressly made subject to the approval of the Court (R. 152).

Creditors are to receive payment of 100% of their allowed claims in the following manner: 20% in notes of the New Corporation, in four notes of 5% each, payable at intervals of six months commencing January 1, 1932; and 80% in the preferred stock of the New Corporation (R. 26, 27). In the event of default in payment of any of the said notes, all of such notes shall, at the option of each holder thereof, become due and payable (R. 27).

The preferred stock is to be issued only and solely to creditors of defendant, pursuant to the plan (R. 21). The holders of preferred stock are entitled to cumulative dividends at the rate of 6% per annum commencing January 1, 1934 (R. 152). The preferred stock is to be placed in the name of two voting trustees for a period of ten years, one of such trustees to be designated by the members of the Creditors' Committee representing merchandise creditors and the other trustee to be designated by the members of the Creditors' Committee representing the bank creditors (R. 28, 29). Voting Trust certificates are to be issued to individual creditors (R. 29).

The New Corporation is authorized to issue one thousand shares of common stock without par value for such consideration as the Board of Directors might deem proper (R. 21). No dividends are to be paid on common stock of the New Corporation until all the outstanding shares of the preferred stock shall have been retired (R. 23).

One-third of the operating profits of the New Corporation for any fiscal year ending after July 1, 1933, must be applied to the retirement of the preferred stock (R. 24). The manner of computing such profits is fixed, and such profits are to be determined by an audit to be made each year by a firm of certified public accountants (R. 24). On dissolution, the par value of the preferred stock and accrued dividends are to be paid in full before any distribution is made to the holders of the common stock (R. 24).

The holders of the preferred stock are entitled to vote solely and as a class upon the creation of priorities or further

preferences among the several classes of stock (R. 22). They are entitled also as a class to vote for the election of two out of the five Directors of the New Corporation until the preferred stock shall have been fully retired (R. 22). Until the notes are fully paid, "the Board of Directors shall have the sole and exclusive right to employ executives of said corporation and to fix the amount of salary as to all of said executives of said New Corporation, and such action of said Board of Directors shall be concurred in by four of the five members of the said Board of Directors" (R. 23).

In order to assure to the creditors the benefit of the services of Morris White, the offer provides that in the event that Morris White shall fail to qualify as president of the New Corporation, or fail to continue as executive in general charge, the holders of the preferred stock "shall have the sole and absolute right as a class to elect three of the New Corporation's directors" (R. 22).

The acceptance of the offer is conditioned upon the filing of a stipulation with the Court by Morris White whereunder he shall agree that he will, for a period of three years, render his sole and exclusive services to the New Corporation, and that he will not at any time during the said period in any way carry on or be connected with any other business or undertaking, except that he shall be free to devote his time and attention to realty enterprises in which he may then have an interest (R. 152, 153).

It is a further condition of the said offer that the New Corporation shall, before the transfer of the assets of the defendant, obtain the release of the receiver from all claims of the Government of the United States and the State of New York against the receiver (R. 153). The New Corporation is required to file a notice of appearance submitting itself to the summary jurisdiction of the Court (R. 29).

On petition of the receiver, an order was signed on May 12, 1931, directing all creditors and any and all other persons interested to show cause at a hearing to be held on the 26th day of May, 1931, why the offer "should not be ac-

cepted and approved by this Court *and at such time and place to consider and act upon any other offer or offers which may then be made*" (R. 15, 16).

The order directed the receiver to mail a copy thereof to all creditors of the defendant and to all parties interested, known to the receiver, on or before May 16, 1931 (R. 16). The offer is part of that order (R. 18). The order further directs the receiver to publish in the New York Times on or before May 15, 1931, a notice briefly stating the provisions of the order (R. 16). Petitioners have stipulated on the record "that the receiver gave due notice of hearing pursuant to the terms of the foregoing order" (R. 16).

Following publication of the notice, several prospective purchasers examined the assets (R. 127), but no other bidder appeared (R. 151). The only offer submitted for the defendant's assets was the offer set forth in the order to show cause. The District Court found as a fact that "no offer other than said offer of Lily White dated April 29, 1931 for the purchase of the assets of the defendant and of the receiver's right, title and interest therein has been made" (R. 151).

The hearing before the District Court began on May 26, 1931 and was continued on the following day (R. 48, 59).

The receiver advised the Court that it was a neutral party to the plan and neither favored nor opposed its adoption (R. 49). The District Court then heard from the creditor body.

The Attitude of the Creditor Body.

Creditors with claims aggregating approximately $850,000 out of the total listed liabilities of $1,072,000 affirmatively voiced their approval of the plan. The creditors' committee had unanimously adopted a resolution recommending approval of that plan (R. 33). That committee directly represented merchandise creditors with claims aggregating $178,000 and bank creditors with claims aggregating $441,500 (*vide supra*, p. 7).

The Government of the United States had filed a claim for $100,000 for taxes, interest and penalties. It expressed its attitude through a special representative, Mr. Cash, sent from Washington, who stated (R. 105):

> "Now, the Commissioner was impressed with the information that this meant the employment of a number of people. Of course, the Commissioner of Internal Revenue is not in the Department of Labor, but using the old term that you don't want to kill the goose that lays the golden egg, the Commissioner wanted to preserve the status of this taxpayer, if he could, so that he could pay future taxes. He has been a very liberal taxpayer; we made investigation there and found that over a period of years, or in recent years these taxes have been paid very liberally by this taxpayer, and we want to preserve it; and like my friend from Boston, I believe the Commissioner expressed the opinion that this man is a genius in this particular work and we feel that the only way to preserve the rights of the creditors and incidentally and also to preserve the rights of the Government, is to permit this new organization and to relieve this man so that he can work out his problems, the problem of paying the Government as well as the ordinary creditors."

And the Government, although entitled to priority, agreed that the tax might be assessed against the New Corporation as transferee and to "take instalments that will not be burdensome" (R. 105).

The State of New York, with a claim for $57,000 due for franchise taxes was willing to enter into a similar arrangement (R. 101).

Vincent Astor, an unsecured creditor in the sum of $47,000, stated through his counsel, Mr. Lyeth, of Carter, Ledyard and Milburn (R. 66-7):

> "May it please the Court, I represent Vincent Astor, the landlord of the premises on which this business has been conducted. Mr. Astor is not a member of the Creditors' Committee, and his claim is not listed among those with the Creditors' Committee. His claim is $47,000

> odd. We have known Mr. Morris White for a great many years, and I say to the Court that we have confidence in his ability to come back. He built up a business from practically, as I understand it, nothing, to a position which in this handbag business is probably second to none in this country, and he had made a great deal of money. * * * My client feels that the only hope of the creditors obtaining any substantial return is to give Mr. Morris White the chance to come back. * * * my client is in favor of the plan; and we have arrived at that conclusion after long discussion with Mr. Morris White individually, and I personally have talked to Mr. Wolinsky, his manager, and I am convinced it is to the best interests of the creditors to accept this offer."

Merchandise creditors not represented on the Creditors' Committee expressed the same view. J. Greenbaum Tanning Co., a merchandise creditor in the sum of approximately $6,000, sent its representative, Mr. Vise, from Chicago. He stated (R. 60):

> "This particular business, as I understand it, is more than a business of buying and selling of merchandise; it involves creative talent, and I believe that Morris White has a great deal of creative talent which can be utilized; and Mr. Tuttle in his argument yesterday objected to the management—the continued management of the business by the same parties. Now, I believe that there should be an amendment to the particular order and decree, providing that Morris White should consent to an injunction, if you please, so that the creditors will have the benefit of his services for a limited time."

The V. S. & M. W. Snyder Co., Inc. (by its representative, Mr. Berman, sent from Boston), a merchandise creditor in the sum of $20,000, which had no representative on the Creditors' Committee, stated (R. 103-4):

> "I represent not only the amount of money; this involves the shut-down of the entire industry and we have got to get started, and if Mr. White does not get started soon, we don't get started and—
>
> The Court: What do you supply?

Mr. Berman: Metal,* sir. As far as our experience has been in matters like this, where, in bankruptcy cases or some similar cases, we never got anything out of it any other way; I don't remember any occasion. We get this talk about the assets; we very seldom get more than 5 per cent at the most, or 10 per cent. And here I know Mr. White, and I don't mind telling you, your Honor, that there is not a second White; never was, and there never will be; not only from my standpoint, but from the standpoint of the entire industry. I have been connected with it, if your Honor please, for at least twenty-seven years, and I remember what it was then what it is now.

The Court: How much did you sell him in the course of a year?

Mr. Berman: Well, we have had the good fortune of selling Mr. White as much as half a million dollars a year; we practically depend upon him; the entire industry lacks confidence to go ahead. * * * And I want your Honor please to remember that it is not just the creditors alone that are involved in it, it is the very future. I don't mind telling you, if, God forbid, anything happened to Mr. White, I would be out of that business—I don't know what I would be doing next—and I am not only myself, but three hundred families in our works—we are shut down; we made up that stock, but what good is it? * * *

And I myself, your Honor, am fearful of the estate, that if it is not handled by a man that understands it, that it is not worth a darn. They can only be utilized by a man that really knows what he is about, and there is no man in New York City who would deny this fact: That Mr. White is Mr. White; that he is not an accident; he didn't get that money by not knowing well; he got that money because—I am proud of the fact, your Honor, to express my opinion for the first time in front of this man, that I was one of them that knows him and understood him—what he said was right; he created that business, just where it was, because it is him; and I am fearful, if your Honor please, for any other way or procedure but to allow him to go ahead; and I can go back home

* The Record (R. 103, 104) indicates that this creditor supplied leather, not metal.

> and put the other boys to work, and we have got just about 5,000 dozen that is finished up to the pickle, ready to go ahead."

Another creditor with a claim of $38,000 and not directly represented on the Creditors' Committee, stated (R. 130):

> "Your Honor, I am one of the creditors for $38,000, and I honestly believe—I never attended any meeting, but I know the concern, and I know just the way this thing is coming around, that unless the creditors work with Mr. Morris White, the creditors would not get a nickel; and I speak as a creditor—I am not protected, I am not insured—let Morris White reorganize his business and get back again and make good so that we will realize some money on it at some future date."

The creditors *affirmatively* recommending the adoption of the reorganization plan, included the United States Commissioner of Internal Revenue, the State of New York and other creditors representing, approximately, 85% of defendant's liabilities. Petitioners' brief (p. 16) refers to the majority of the creditor body which approved of the plan of reorganization as a "well organized claque". This imputation is supported only by the assertion of petitioners' counsel. It was accepted neither by the District Court nor by the Circuit Court of Appeals. It is not supported by the record. It does appear on the record that the plan of reorganization was approved by 98% of defendant's 250 creditors. They desired to preserve the demonstrated value of defendant's good will, as to which the Circuit Court of Appeals said (R. 166):

> *"It was established in the court below that Morris White, Inc., consistently made profits averaging about $500,000 per year, which demonstrated a good will not valued."*

On the basis of that good will, the reorganized corporation within two years would have been able to discharge in full its $1,000,000 of liabilities.

The Opposition.

The Court specifically invited an expression of opinion from creditors opposing the plan (R. 92):

> "I want to ask if there is any one here who is opposed to this plan other than those who have already spoken."

All 5 petitioners had theretofore expressed their opposition to the plan. There were no other dissenters. Out of approximately 250 of the defendant's creditors, the petitioners were the only opponents.

The petitioner, Herman Loewenstein, is a merchandise creditor with a claim of $5600 (R. 60). The petitioner, G. Levor & Co., Inc., is a judgment creditor with a claim of $4500 (R. 65).

The petitioners, National Surety Company, American Credit Indemnity Co., and London Guarantee and Accident Company, Ltd., are not direct creditors of the defendant. Unlike the other creditors they had done no business with the defendant. Their claims arise out of credit insurance policies issued upon various merchandise accounts with the defendant (R. 135-7).

Claims aggregating $92,138.15 had been filed against the surety companies (R. 167). Included among those claims was the above mentioned claim of G. Levor & Co., Inc. (R. 136) upon which the National Surety Company denied liability (R. 65, 66). The policies of credit insurance purported to cover only part of the accounts insured (R. 129). Counsel for the surety companies, although the Court requested them to do so, were unable to state either the approximate or the maximum amount of the contingent liabilities upon policies which had been issued (R. 129). On the hearing, counsel for the Surety Companies stated: "The only claim paid is that $19,000 claim" (R. 129).

Counsel for dissenting creditors referred at the hearing to "persistent rumors of side agreements" between the defendant and creditors (R. 106) and asked for leave to submit

affidavits with respect thereto (R. 117). The affidavits thereafter submitted by petitioners contained no reference to any such "side agreements" (R. 135-141). And when counsel for dissenting creditors were given an opportunity to examine Mr. White as to any such agreements, one of them said (R. 107):

> "I have no information as to any side agreements. It would be a fishing expedition, as far as I am concerned."

Prior to the hearing, petitioners' counsel made no attempt to obtain any information from the receiver or the receiver's counsel or the Creditors' Committee (R. 63-4, 71, 123, 125). Requests for information made at the hearing by petitioners' counsel were complied with; an inventory was available and every question that was asked was answered (R. 107, 126, 127, 128). The court examined Morris White under oath (R. 118) and then submitted him for examination to the creditor body (R. 121). Counsel representing one of the petitioners did examine Mr. White (R. 121).

The Decision of the District Court.

At the close of the hearing in the District Court, Judge KNOX rendered his decision in favor of the acceptance of the offer (R. 130-132), subject to certain modifications. Those modifications were, in substance, as follows (R. 152-3):

> (1) That dividends on the preferred stock be cumulative commencing January 1, 1934.
>
> (2) That all allowances and fees for services rendered in the proceedings, payable out of the estate, "shall be subject to the approval of this Court."
>
> (3) That Morris White stipulate and consent, under injunction, to render his exclusive services to the New Corporation for a period of three years.
>
> (4) That the New Corporation stipulate in proper form to assume payment of the amounts due for State and Federal taxes.

In his opinion, Judge KNOX stated (R. 130-131):

> "That if the estimate of value which has been placed upon the assets of the defendant corporation is anywhere near correct, it means, if this concern goes into liquidation, that the general creditors will get little or nothing as a result, due to the fact that machinery, such as I imagine is contained in that place, would bring only junk prices, and that the silks and leather that might be devoted to the manufacture of ladies hand bags, would be little more than remnants and that it would be bought at a highly depreciated value by whomsoever might wish to enter this business; and that the priority claims, such as the Federal Government's taxes, and the State Government taxes, would take practically all that might be realized from such a sale. The experience that I have had in seeing businesses such as this liquidated has been of a character as to lead me to believe that not much is to be hoped for from that standpoint; and that in addition to the small sum of money that would probably be derived from such a sale, there would have to be deducted the expenses of administration; the auction sale of the assets would be an expensive matter, in the way of lotting, I should think; and that if liquidation takes place I should be surprised if creditors would realize more than between 5 or 10 percent, at the utmost."

Judge KNOX, in his decree of June 15, 1931, approving the offer, made the following findings of fact (R. 151-2):

> "3. No offer other than said offer of Lily White dated April 29th, 1931 for the purchase of the assets of the defendant and of the Receiver's right, title and interest therein has been made.
>
> 4. The value of the assets of the defendant upon the basis of liquidation by the Receiver is substantially less than the value of such assets on a going concern basis.
>
> 5. The general creditors of defendant will realize only a small recovery upon their indebtedness if liquidation by the Receiver is had.
>
> 6. Continuance of the business under the plan embraced in the said offer of Lily White would enable the

preservation of the difference between the liquidation value of the assets of defendant and the value of said assets on a going concern basis and would enable the preservation of the value of the good will of defendant.

7. Continuance of the business under the plan embraced in the said offer of Lily White would afford the general creditors a better opportunity to recover the indebtedness owing them than they would have if such assets were now to be liquidated.

8. Said offer is fair and equitable to all of the creditors of defendant and its acceptance upon the terms herein stated is in the best interests of such creditors."

The Decision of the Circuit Court of Appeals.

Petitioners appealed to the Circuit Court of Appeals for the Second Circuit from the District Court's order (R. 157, 159).

The gist of petitioners' objections in the Circuit Court of Appeals is stated in the opinion of that Court as follows (R. 168):

> "The question presented to us is whether these minority creditors are obliged to accept the plan, taking stock and notes in place of cash, and be contented to wait the outcome of this new venture in the hope that some day the preferred stock will be redeemed and payment of their notes made. Have the appellants been deprived of their rights as creditors by this order?"

The Circuit Court of Appeals held that the order of the District Court, in so far as it deprived objecting creditors of the payment in cash for their *pro rata* interest in the defendant's assets, was improper and reversed the order to that extent. It held (R. 173):

> "An outstanding circumstance is the willingness of the majority of creditors to proceed with this reorganization, expressing the view, as they did in the court below, that the rehabilitation of White's business gave the best promise for the payment of their debts. * * * But the minority creditors, appellants, insisting upon the right

to share immediately in the proceeds of a forced sale of the corporation's assets, have dissented. Their rights must be protected. They are ordinarily entitled to a public sale with competitive bidding, the assets to be sold to the highest bidder. They have a just claim to their proportionate share of the price which would have been realized at such sale after deduction of administration expenses. If a court of equity can protect these rights and at the same time carry out the wish of the other creditors, who favor the plan of reorganization, it should be done. The reorganization plan has been put into operation, and creditors, excepting the appellants, are content to have it proceed. We think both may be protected."

The Circuit Court of Appeals directed that the appellants be paid their distributive share of the assets in cash (R. 173-4):

"The appellants will be fully protected by having an appraisal of the value of their respective claims made before a master, to be appointed, who will take an account of the assets and liabilities of Morris White, Inc., ascertaining the value of the assets as if sold at a public sale. * * * In this way, from the ascertained sum of money that would have been realized, had a sale taken place, the appellants may be awarded their aliquot shares of the assets. This sum must be paid in cash, or, at the option of each of the appellants, the preferred stock and notes offered to them may be valued as of the date the reorganization plan became effective, and that sum paid in cash to them or either of them. * * * If payment is not thus made in cash, the several amounts which appellants are found entitled to may be collected by a sale of the property transferred to the new corporation. * * * There will thus be preserved to appellants their right to payment in cash, and it removes the objection they properly raise. The remaining creditors, satisfied with the plan, are then free to proceed with its operation."

The Circuit Court of Appeals in its opinion further said (R. 173):

> "The appellants should have full opportunity to question any preference that may have been made. The banks should not collect on the security which has been pledged as collateral, and, in addition thereto, receive preferred stock. They may agree to accept preferred stock and notes for such sums as they do not realize upon the sale of the collateral up to the amount of their respective claims, but no more."

The order of the Circuit Court, now under review, provides (R. 175):

> "* * * that the order of said District Court be, and it hereby is, reversed, with costs and cause remanded to the District Court for further proceedings in accordance with the opinion of this Court."

The basic assumption upon which the Circuit Court of Appeals reversed the decree of the District Court is that the District Court lacked power in an equity receivership of a private corporation to compel creditors to accept anything other than cash in satisfaction of their claims. The Circuit Court further assumed that the plan of reorganization approved by the District Court was inequitable in that it permitted secured creditors to prove the full amount of their claims and to receive dividends thereon. In both assumptions the Circuit Court of Appeals erred.

ARGUMENT.

FIRST POINT.

The decree of the District Court dated June 15, 1931, approving the plan of reorganization, was a proper exercise of the power and discretion of that Court. Modification of that decree by the Circuit Court of Appeals awarded to the petitioners something more than that to which they were properly entitled and they may not now complain that greater special privileges were not granted to them.

1. *Respondents are properly entitled to assert the validity of the decree of the District Court for the purpose of sustaining the decree of the Circuit Court of Appeals.*

This is settled by recent decisions of this Court.

> *Langnes* v. *Green* (1931), 282 U. S. 531, 538;
> *Story Parchment Co.* v. *Patterson Parchment Paper Co.* (1931), 282 U. S. 555, 560.

In the latter case, Mr. Justice SUTHERLAND, delivering the opinion of the Court, stated:

> "Respondents seek to sustain this judgment upon that ground and also upon the additional ground, which the lower court found against them, that there was no evidence of a conspiracy or combination to monopolize interstate trade. *Because there was no cross petition for certiorari, petitioner insists that the additional ground is not open here for consideration. But respondents do not invoke that ground in order to overthrow the judgment below, but to sustain it; and this they may do.** Langnes v. Green, 282 U. S. 531 * * *."

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* Italics here and in all subsequent quotations are ours, unless otherwise indicated.

If the decree of the District Court, dated June 15, 1931, was a proper exercise of the power and discretion of that Court, petitioners cannot complain of the decree of the Circuit Court of Appeals which gives to petitioners greater rights than the decree of the District Court.

2. *The District Court had power to direct the sale of defendant's assets upon terms that provided for satisfaction of the claims of unsecured creditors by notes and preferred stock. The power of the Federal Courts in equity receiverships to compel creditors to accept something other than cash in satisfaction of their claims is firmly established.*

Such power has grown out of the administration of a trust imposed upon the Court. We have found no better specification of the character and extent of that trust than that of Circuit Judge WALTER H. SANBORN in *Phipps* v. *Chicago, R. I. & P. Ry. Co.* (1922, C. C. A. 8th), 284 Fed. 945.

He said that, upon the appointment of the receiver (p. 949):

> "* * * that court [the District Court] held all that property [of the defendant] in trust, subject to the liens of the secured creditors, to operate it and to distribute it or its proceeds to all the unsecured creditors and all the stockholders of the insolvent company according to the respective ranks and equities of their claims. Every unsecured creditor then and thereafter was a cestui que trust of the court, entitled to a like interest in the property in proportion to the amount of his claim, as every other such creditor and every stockholder was a cestui que trust of the court, entitled to a like interest in the property in proportion to the amount of his stock to that of every other stockholder. When that court had so operated the property, and by its decree had so distributed either the property itself or its proceeds, it had faithfully executed its trust and rendered the right decree."*

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* Matter in brackets here and in all subsequent quotations ours, unless otherwise noted.

The question presented is whether, in executing and carrying out the trust imposed upon the Court in the case at bar, Judge KNOX had power to require a small group of dissenting creditors to accept in satisfaction of their claims securities in the reorganized company.

The *power* of the Federal Courts in equity receiverships to compel creditors to accept something other than cash in satisfaction of their claims is established by decisions of this Court. In *Northern P. R. Co.* v. *Boyd* (1913), 228 U. S. 482, attack was made upon the sale of assets pursuant to a plan of reorganization. The sale and reorganization had been held invalid by the Courts below because stockholders were inequitably preferred to creditors. The late Francis Lynde Stetson, counsel for the Railway Company, the appellant in this Court, argued that the approval of Boyd's contention would require payment in cash to all dissenting creditors and that this would make reorganizations impossible. The Court rejected this argument, declaring in its opinion, at page 508:

> "*This conclusion does not, as claimed, require the impossible, and make it necessary to pay an unsecured creditor in cash* as a condition of stockholders retaining an interest in the reorganized company. *His interest can be preserved by the issuance, on equitable terms, of income bonds or preferred stock.* If he declines a fair offer, he is left to protect himself as any other creditor of a judgment debtor, and, having refused to come into a just reorganization, could not thereafter be heard in a court of equity to attack it."

Petitioners' brief (p. 32) refers to the foregoing language of this Court in *Northern P. R. Co.* v. *Boyd, supra,* as a *dictum.*

That the language used by this Court in the *Boyd* case embodies the deliberate and considered opinion of the Court is conclusively settled by its subsequent decision in the case of *Kansas City Terminal R. Co.* v. *Central Union Trust Co.* (1926), 271 U. S. 445. The District Court, on a creditors' bill, had appointed a receiver in equity. The assets of

the defendant were purchased by a creditors' committee pursuant to a plan of reorganization. The reorganization plan offered to unsecured creditors the alternative of (a) one-third share of preferred stock, $100 par value, and two-thirds share of common stock, without par value, for each $100 of their allowed claims, or (b) $20 in bonds and one share of common stock, upon payment of $18 (271 U. S. at p. 452). The District Court overruled objections of dissenting creditors. The matter went to the Circuit Court of Appeals for the Eighth Circuit. The Circuit Court certified questions to this Court for instructions.

This Court, answering the questions certified, stated (271 U. S. at p. 454):

> "This doctrine is the 'fixed principle' according to which Northern P. R. Co. v. Boyd (p. 507 (57 L. Ed. 943, 33 Sup. Ct. Rep. 554)), declares the character of reorganization agreements must be determined; and to it there should be rigid adherence. But as that opinion states, this does not require the impossible and make it necessary always to pay unsecured creditors in cash before stockholders may retain any interest whatever in the reorganized company. By way of illustration it further pointed out, that such creditors can be protected 'by the issuance, on equitable terms, of income bonds or preferred stock.' And we now add that, when necessary, they may be protected through other arrangements which distinctly recognize their equitable right to be preferred to stockholders against the full value of all property belonging to the debtor corporation, and afford each of them fair opportunity, measured by the existing circumstances to avail himself of this right."

Upon the answers made to the questions certified, the Circuit Court of Appeals for the Eighth Circuit sustained the validity of the plan. *Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.* (1928), 28 F. (2d) 177.

In accordance with the doctrine enunciated in the *Boyd* case, and reaffirmed in the *Kansas City Terminal Ry.* case, there have been numerous decrees of sale in equity re-

ceiverships upon terms which compelled creditors to accept notes, preferred stock or common stock of the reorganized company in satisfaction of their claims.

In *St. Louis-San Francisco Ry. Co.* v. *McElvain* (1918, D. C. E. D. Mo.), 253 Fed. 123, the Court sustained the validity of a sale of assets pursuant to a plan of reorganization. The reorganization plan provided that unsecured creditors receive $50 par value 6% non-cumulative preferred stock and $50 par value common stock for each $100 of duly allowed claims. The order confirming the sale was made over the objections of dissenting creditors (253 Fed. at p. 126).

The validity of the plan of reorganization in the *St. Louis-San Francisco Ry.* case, *supra,* was upheld by this Court in the case of *St. Louis & S. F. R. Co.* v. *Spiller* (1927), 274 U. S. 304. In that case, Spiller, a creditor of the St. Louis-San Francisco *Railroad* Company obtained a judgment after the sale under the reorganization plan. Spiller attacked the validity of the sale, seeking to charge the property of the defendant acquired by the new company with the amount of his judgment. This Court held that the plan was a fair plan and that Spiller was bound thereby (274 U. S. pp. 313 *et seq.*).

In *Phipps* v. *Chicago, R. I. & P. Ry. Co.* (1922, C. C. A. 8th), 284 Fed. 945, the Court sustained the validity of a decree in an equity receivership which required all unsecured creditors to accept 6% preferred stock to the amount of their claims, together with interest at the rate of 5% in cash, and barred them from asserting any further claim against the defendant corporation (284 Fed. at p. 947). Phipps had sued the Railway Company for damages for personal injuries, and obtained a judgment for $7,000 in the State Court of Missouri. After the termination of the receivership, he caused an execution to be issued upon his judgment against the assets of the Railway Company and sought to attach and garnishee amounts owing to that Company. Immediately upon the issuance of the attachment by Phipps, the Railway Company applied to the United

States District Court in Missouri, at the foot of its ancillary decree, for an injunction against the enforcement by Phipps of his judgment against the Railway Company.

The case squarely raised the question of the Court's power to compel dissenting creditors to accept securities in satisfaction of their claims. Judge WALTER H. SANBORN, writing the Court's opinion, said, at page 949:

> "Every unsecured creditor then and thereafter was a *cestui que trust* of the Court, entitled to a like interest in the property in proportion to the amount of his claim, as every other such creditor and every stockholder was a *cestui que trust* of the Court, entitled to a like interest in the property in proportion to the amount of his stock to that of every other stockholder * * * *Nor was it indispensable to such a just result, or to a lawful decree that the interest or share of any of the cestuis que trust should be secured or paid to him or it in cash. It was within the power and the judicial discretion of the court to adjudge and secure that interest or share to him or it in the stock, bonds, or other securities of the reorganized company.*"

In *P. R. Walsh Tie & Timber Co. v. Missouri Pac. Ry. Co.*, (1922, C. C. A. 8th), 280 Fed. 38, the Court upheld a plan of reorganization which provided (see p. 43) that general creditors of the defendant should receive convertible 5% preferred stock equal to the amount of their respective claims.

The foregoing cases establish the *power* of the Court in an equity receivership to compel creditors to accept something other than cash in satisfaction of their claims. Admittedly these cases relate to receiverships of railroads and other semi-public corporations. The defendant in the cause at bar was not in that category. There is, at least, a suggestion in the opinion of the Circuit Court (R. 171) that this difference limits the power of the Court and dictates a different rule with respect to private corporations. The fact that a corporation is a public utility may permit a broader regulation of that corporation's activities. That is not the question in this case. We are here concerned with the power

of the Court in an equity receivership to compel creditors to accept something other than cash.

3. *That power exists in a receivership of an industrial corporation as well as in a receivership of a public utility corporation. The exercise of that power is a matter within the discretion of the Court.*

If there is any basis for the contention that the dissenting creditor has an absolute right to cash, *it must rest in the creditor's right—not in the character of the corporation* in which he has an interest. If a creditor has the right to cash, we can conceive no reason why he should not have it as much against a railroad, gas or electric light company as against the United States Steel Corporation or the General Electric Company. The rights of creditors of private corporations are no more sacred than are the rights of creditors of public utilities. If a different rule does exist with respect to private corporations, that difference must relate not to jurisdiction but to the exercise of jurisdiction, not to power but to policy.

There is no constitutional prohibition against the exercise of the same powers in an equity receivership of an industrial corporation as are exercised in an equity receivership of a public utility. There is nothing in Article I, Section 10, Clause 1, of the Constitution of the United States, cited in the opinion of the Circuit Court of Appeals (R. 169), which requires that, in an equity receivership of a private corporation, creditors must be paid in cash. That provision of the Constitution, in so far as relevant, is to the effect that:

> "No State shall * * * make any Thing but gold and silver Coin a Tender in Payment of Debts; * * *."

This is a provision against legislation by the several States; and the case of *Farmers & M. Bank* v. *Federal Reserve Bank* (1923), 262 U. S. 649, cited by Judge MANTON (R. 169), relates to such legislation. That provision of the Constitution does not purport to restrict the powers of a

Court of equity, nor does it make any distinction between public and private corporations. The "due process" clause does not touch the matter, in the existing state of the decisions. This Court has specifically held that a dissenting creditor has no inherent right to be paid in cash upon reorganization. The question of what is "due process" in the equity Court has thereby been settled for creditors of industrial corporations as well as for creditors of railroads.

There is no direct or decisive authority which denies the jurisdiction of a Court of equity in receiverships of private corporations to compel creditors to accept a fair equivalent of their claims in something other than cash. We do not question the correctness of the decision of Judge LEARNED HAND (then District Judge) in *Re Prudential Outfitting Co.*, (1918, D. C., S. D., N. Y.) 250 Fed. 504, or the opinion of Judge MCPHERSON in *Re Northampton Portland Cement Co.* (1911, D. C., E. D., Pa.), 185 Fed. 542, which are quoted in petitioners' brief (pp. 29, 30) and are cited in the opinion of the Circuit Court of Appeals (R. 171). These cases relate to a sale of assets in bankruptcy and the restrictions of the Bankruptcy Act are applicable thereto. Nor are we here concerned with cases dealing with special statutory provisions governing liquidation of an insolvent national bank, such as that of *Re Sale of Assets of First Nat. Bank of Florence* (1925, D. C., E. D., S. C.), 6 F. (2d) 905, a case cited both in petitioners' brief (p. 30) and in the opinion of the Circuit Court of Appeals (R. 171).

There is language in *Harding* v. *American Sumatra Tobacco Co.* (1926, D. C., N. D., Ga.), 14 F. (2d) 168, which expresses a doubt about the existence of this power in the receivership of an industrial corporation, but that language is pure *dictum*. The decision rests upon the ground (p. 170) that the Court lacked jurisdiction over the subject matter.

The element of a "public interest" involved in the "utility" receiverships has no bearing on the question of the rights of creditors. But, assuming that it has, the factual basis for the distinction between utilities and industrial corporations

is lacking in our present regime of "big business". The element of public interest which is involved in the continued operation and reorganization of a railroad or other semi-public corporation, may also exist in the case of industrial corporations. The disruption of large industrial corporations affects the public as vitally as the so-called "utilities". The public now has the same large investments in these huge industrial companies that it has in the "utilities". It has the same vital need for what it gets from the industrial corporation as for that which the "utility" companies furnish it. If the United States Steel Corporation or the General Electric Company should cease to function the public would suffer as much as if a street car company suspended its operations.

The business of the defendant in the case at bar involved no such great public interest as that of the United States Steel Corporation. Nevertheless, the defendant was the leader in its particular field of industry. Prior to this receivership, it had done an average business in excess of $5,000,000 a year. It employed between three and four thousand people. When the defendant's business ceased to function, that entire industry came to a standstill. As one creditor stated:

> "* * * this involves the shutdown of the entire industry and we have got to get started, and if Mr. White does not get started soon, we don't get started. * * *" (R. 103).

Certainly, the public interest demands that industry and business shall be continued in operation, wherever possible. Industrial enterprises, large and small, are today in dire financial difficulty. To destroy such enterprises by forced liquidation for cash, because a single creditor demands it, is to disregard the rights of the majority of the creditor-body who favor reorganization, and to ignore the present demands of public interest.

The wisdom of the establishment of this power of a Court of equity on reorganization to compel dissenting creditors to

accept something other than cash, is emphasized and exemplified by the financial and commercial troubles that now beset us. This Court, very recently, has taken judicial notice of the depression and commented on its vital importance in dealing with present problems. The Court said in *Atchison, T. & S. F. R. Co.* v. *United States* (1932), 284 U. S. 248, speaking by the Chief Justice (p. 260):

> "There can be no question as to the change in conditions upon which the new hearing was asked. *Of that change we may take judicial notice. It is the outstanding contemporary fact, dominating thought and action throughout the country.*"

The Court thus knows, quite as well as any of the rest of the world, that markets for things to be sold have disappeared as a practical matter. Everyone with any practical knowledge of existent conditions knows that an owner of real estate today cannot find a buyer for it at any price worth calling a price, and that countless creditors of such real estate owners are faced with exactly the same problems and the same limitations that the creditors of Morris White, Inc., had to face on this receivership. The condition of the real estate market is only typical of what exists in every other field of business or commercial activity. The Court knows, too, that, as a concomitant of this inability to sell things, the obtaining of cash in any appreciable amount is an undertaking beyond the power of most of us. And, it is hardly necessary to add, Judge KNOX was quite as cognizant of these difficulties as this Court has announced itself to be.

Such considerations, which the economic conditions drive home to us so irresistibly, demonstrate forcefully the wisdom of this Court in announcing, as it has in the *Boyd-Northern Pac.* and *Kansas City Terminal* cases, that the discretion of the District Court in executing the trust imposed on it in these equity receivership cases, is not to be limited by any unyielding and drastic requirement that cash must be paid to dissenting creditors upon reorganization. In the existing

circumstances, it is practically impossible to get cash. The expedients available in ordinary times and conditions for raising cash to pay dissenting creditors are not now available. Though the majority of the creditors and stockholders may desire reorganization they cannot contribute cash for that purpose. A cash limitation on the exercise of the discretion of the Court in these matters would be tantamount to a decree that no reorganizations can be put through during the continuance of the depression.

The present Bankruptcy Act does not afford the requisite machinery to meet this need. It is the defects of this Act which have given rise and impetus to the potent movement now under way to amend the Bankruptcy Act by adding specific provisions permitting such reorganizations in bankruptcy proceedings. The Court will, doubtless, recollect the recommendations of the Solicitor General to this effect, based upon somewhat similar provisions in the English Act.

The Solicitor General's report on this matter, bearing date of December 8, 1931, appears as an appendix to the President's special message to Congress under date of February 29, 1932. In Part IV of that Report, entitled "Remedies", the Solicitor General speaking of the defects of the present Bankruptcy Act says (p. 39):

> "Instead of affording relief to debtors before their affairs have been completely ruined in financial failure, *the Act insists upon liquidation or a cumbersome process of composition* and no practical method is provided for saving debtors from ruin without branding them as bankrupts.
>
> "We have concluded, therefore, that *the Act should be amended so as to provide remedial process* in voluntary proceedings under which debtors, unable to pay their debts in due course, may have the protection of the Courts, without being adjudged bankrupt, *for the purpose of composing or extending the maturity of their debts, amortizing the payment of their debts out of future earnings*, procuring the liquidation of their property under voluntary assignments to a trustee, *and in the case of corporations for the purpose of a reorganization.*"

The details concerning these suggestions are discussed at length in the appendix to the Solicitor General's Report.

On page 90, *et seq.*, "Corporate Reorganizations" are discussed. The Solicitor General says (p. 90):

> *"The process of liquidation in bankruptcy is in most cases essentially destructive of these interests* [those of the public in the corporation], *because it can not preserve the value of a going concern."*

A new Section of the Bankruptcy Act is recommended for the reorganization of corporations. The Solicitor General characterizes this proposed amendment as follows (p. 90):

> "Proceeding upon the principle applied in compositions, that *the views of a substantial majority of the creditors should control* the measures to be adopted for the protection and preservation of their rights in the failing business, subject at all times to a finding by the Courts that what they propose is fair and equitable to the minority, the proposed amendments not only afford a simple, prompt, and effective process of reorganization, but they are carefully drawn to adequately preserve the rights of lien holders and other creditors, who appear and insist upon such relief, *to have their interests fairly appraised and liquidated by cash payments."*

Our adversaries suggest that a reorganization of the sort we are discussing could be put through in a bankruptcy proceeding under the provisions in the existing Bankruptcy Act for compositions (Sec. 12). And it could be, if the situation afforded the time to follow through what the Solicitor General has accurately defined as the "cumbersome process" (see p. 35, *supra*), for which the present Act provides. In composition proceedings, such persistingly dissentient creditors as the petitioners in the case at bar can delay and postpone the approval and execution of a composition plan for a long time if they set out with that end in view. With the procedure required under that Section—the examinations and objections available to objectants under the com-

position provisions of the present Bankruptcy Act—it may be months before the plan can be carried out. Such delay is all too often fatal.

Under existing conditions, the only proceeding available to the creditors of corporations in distress who desire a reorganization to preserve their interests, and do not want the business to be sold under the hammer at a ruinous sacrifice, is this equity receivership. Its availability in such difficult times as those now existing, is due to the wise determination of this Court, that an unreasonably dissenting creditor can not prevent a reorganization because cash cannot be obtained for him in such a time of chaos.

There is another consideration to be thought of in dealing with this contention for the cash limitation of the equity Court's power in executing the trust imposed upon it in equity receiverships. This consideration comes about from the changed conditions in the commercial world. Individualism in business is an outworn dogma. Every merchant who sells goods to another today, every banker who loans money to the merchant, every workman who sells the merchant his labor—in short, every person of any sort who has dealings with the merchant knows that he is one of tens or hundreds or thousands who are dealing with the merchant just as he himself has done. He knows that the interests of these others are as inextricably intertwined with those of that merchant as his own. He knows, or he ought to know, that he cannot exact his "pound of flesh" from the merchant without undue injury to the others, similarly situated to himself. And the Courts know this quite as well as the members of the mercantile or banking world. They appreciate thoroughly the necessity—for it is that now!—for creditors to work together, especially when it comes to salvaging what they can out of a financial or commercial wreck. They understand, too, the impossibility of allowing a single creditor, or a small group of dissenting creditors, to prevent the vast majority of creditors from adopting and carrying out what they believe to be the best means of salvage. With this

change in the character of commercial and financial dealings, the general policy of the law must be, to limit the power of the vastly predominating majority of the creditors as little as is consistent with the preservation of those ultimate individual rights which are inherent in our system.

The petitioners have characterized the equity Court, exercising the power to approve a reorganization without cash to the dissenter, as a "benevolent despot" and an "absolute autocrat". We believe we have dissipated any idea of that sort in what we have said above. But it may be permissible to call the Court's attention to the character of the position which the dissenting creditor would occupy if the contentions of petitioners should prevail. The dissenting creditor would then truly occupy the role of "absolute autocrat". He would then be in a position to dictate not only to the other creditors but also to the Court. Everyone else—creditors and Court—may believe that the best chance of salvage is to be found in the reorganization venture, without cash. He differs, and, if the petitioners' argument is sound, his view must control. This smacks of "despotism" and "autocracy", and of a kind not suited to the needs and temper of our times!

4. *The plan approved by the District Court gave fair recognition to the rights of creditors and stockholders of the defendants, according to the respective ranks and equities of their claims and, therefore, complies with the "fixed principle" enunciated in the Boyd case* (228 U. S. 482).

(A) *The "fixed principle" of the Boyd case merely requires that the reorganization plan shall give recognition to creditors and stockholders substantially in accordance with the respective ranks and equities of their claims.*

The reorganization considered in the *Boyd* case made no provision whatsoever for unsecured creditors (228 U. S. 482, 504). This Court held (pp. 507, 508) that the plan was unfair, not because it gave to stockholders an interest in the reorganized company but, rather, because it made no offer of

participation to unsecured creditors and failed completely to recognize the superior equity of creditors. As was said by Judge SANBORN in *Phipps* v. *Chicago, R. I. & P. Ry. Co.*, 284 Fed. 945, at 948:

> "The vice which rendered the foreclosure, judicial sale, and delivery of the property to the reorganized corporation voidable by unsecured creditors in the *Boyd Case*, 177 Fed. 804, 101 C. C. A. 18, Id., 228 U. S. 482, 502, 504, 33 Sup. Ct. 554, 57 L. Ed. 931, and in the *Kansas City Southern Railway Co. Case*, 240 U. S. 166, 36 Sup. Ct. 334, 60 L. Ed. 579, was not the lack of judicial sales of the property under the decrees, but the fact that *under the plans of reorganization and by the decrees in those cases the stockholders of the insolvent corporations were given for their stock beneficial interests in the reorganized companies* by way of stocks, bonds, or other securities, *while the unsecured creditors of the insolvent companies were given nothing.*"

That vice does not inhere in the present plan of reorganization.

(B) *The plan of reorganization approved by the District Court in the present case makes fair provision for creditors. It fairly recognizes the superiority of their rights over the rights of stockholders of the defendant corporation and provides for the payment of their claims in full.*

Under the plan of reorganization, creditors receive, in lieu of their claims as proved and allowed, 20% in the notes and 80% in the preferred stock of the reorganized corporation (R. 26-7). One-third of the annual operating profits of the business must be devoted to the retirement of preferred stock (R. 24). Cumulative dividends, at the rate of 6% per annum, are payable on the preferred stock commencing January 1, 1934 (R. 152). No dividends are to be paid on the common stock until all preferred stock shall have been retired (R. 23). On dissolution, the par value of the preferred stock and accrued dividends are to be paid in full before any dis-

tribution is made to holders of common stock (R. 24). The rights of the stockholders of the old corporation, through ownership of the common stock of the reorganized corporation, are thus subordinated to the prior payment of the notes and preferred stock issued to creditors. All the stockholders of the old corporation receive is a reversion after the creditors are paid in full. The plan recognizes the superior right and rank of the claims of the unsecured creditors, provides for the satisfaction of those claims in full and, therefore, fully complies with the "fixed principle" of the *Boyd* case.

(C) *The plan does not violate the "fixed principle" of the Boyd case in permitting stockholders of the defendant to retain a reversionary interest in the New Corporation, represented by the common stock.*

Petitioners argue that the issuance of common stock of the reorganized company to stockholders of the old company, constitutes a violation of this "fixed principle". Petitioners misconceive the "principle". In the *Boyd* case, this Court said (228 U. S. at p. 508):

> "This conclusion does not, as claimed, require the impossible, and make it necessary to pay an unsecured creditor in cash *as a condition of stockholders retaining an interest in the reorganized company.* His interest can be preserved by the issuance, on equitable terms, of income bonds or preferred stock."

In *Kansas City Terminal R. Co.* v. *Central Union Trust Co.*, 271 U. S. 445, this Court, after discussing the "fixed principle" announced in the *Boyd* opinion, said, at page 454:

> "But, as that opinion states, this does not require the impossible and *make it necessary always to pay unsecured creditors in cash before stockholders may retain any interest whatever in the reorganized company.*"

In these cases, the Court has held that the superior rights of creditors can be fairly recognized and dealt with by the

issuance to them of bonds or preferred stock. The old stockholders may be permitted to retain the reversionary interests which is what the common stock represents. Therefore, the issuance of common stock to stockholders of the old corporation is not a violation of the "fixed principle".

(D) *The grant of the limited right to the holders of common stock to elect a majority of the board of directors does not violate the "fixed principle" of the Boyd case.*

This Court has held that bonds or preferred stock may be issued to satisfy the creditors' rights. Bonds or preferred stock rarely, if ever, carry with them control of the corporation or even voting rights. That control usually rests with the common stock. Under the "fixed principle" the common stock may be given to the old stockholders if the rights of creditors are otherwise recognized in some equitable manner.

The question as to what control the creditors, as preferred stockholders, should exercise over the affairs of the new corporation was a matter for the business judgment of the creditor body. The preferred stock is entitled to elect two of the five directors until the preferred stock is fully retired (R. 22). The reorganization plan provides that if Morris White failed to continue as executive in general charge of the business of the reorganized corporation, the preferred stockholders are entitled to elect a majority of the board of directors (R. 22). The plan further provides that, until the promissory notes issued to creditors under the plan are fully paid, the board of directors shall have the exclusive right to employ executives of the new corporation and that the vote of four directors shall be required for this purpose (R. 23). Thus the consent of one of the two directors representing the preferred stock is required to give the common stock the right to elect a majority of the board of directors.

It was the desire and will of the great majority that Morris White remain in control of the new corporation (R. 109). It was the opinion of creditors that his ability constituted a most valuable asset of the business (R. 60, 103). The creditors

knew they could not run the business (R. 109). They did not want to run the business (*id.*). They believed that the services of Morris White were essential for that purpose (R. 103-4). Indeed, Judge KNOX, as a condition of the approval of the plan of reorganization, required that Morris White consent to an injunction compelling him to render his services exclusively to the reorganized corporation for a period of three years (R. 152-3). The great majority of the creditor body and the District Court believed that the interests of creditors required the management of the business to remain in the hands of Morris White. It is not for the minority, whose superior rights have been fairly recognized by the issuance of preferred stock and notes, to dictate to the great majority of the creditor body with respect to the control and the business policy of the new corporation.

(E) *The reorganization plan, in so far as it permitted secured creditors to prove and collect dividends on the full amount of their claims, merely recognized an established rule of equity with respect to the rights of secured creditors.*

The Circuit Court of Appeals, in its opinion (R. 173), intimated that the plan of reorganization gave an improper advantage to secured creditors. It held that secured creditors were entitled to receive "preferred stock and notes for such sums as they do not realize upon the sale of the collateral up to the amount of their respective claims, but no more" (R. 173). In this the Circuit Court erred. It is settled beyond question that in equity a secured creditor is entitled to prove for the full amount of his claim and to collect dividends thereon up to the full amount of any deficiency. That rule was recognized by this Court in *Merrill* v. *National Bank of Jacksonville* (1889), 173 U. S. 131. In that case the Chief Justice (FULLER), speaking for the Court, said at page 146:

> "We repeat that it appears to us that the secured creditor is a creditor to the full amount due him when the insolvency is declared, just as much as the unsecured creditor is, and cannot be subjected to a different rule.

> And as the basis on which all creditors are to draw dividends is the amount of their claims at the time of the declaration of insolvency, it necessarily results, for the purpose of fixing that basis, that it is immaterial what collateral any particular creditor may have. The secured creditor cannot be charged with the estimated value of the collateral, or be compelled to exhaust it before enforcing his direct remedies against the debtor, or to surrender it as a condition thereto, though the receiver may redeem or be subrogated as circumstances may require."

and further stated at page 147:

> "Our conclusion is that the claims of creditors are to be determined as of the date of the declaration of insolvency, irrespective of the question whether particular creditors have security or not. When secured creditors have received payment in full, their right to dividends, and their right to retain their securities, cease, but collections therefrom are not otherwise material."

The principles above stated are now settled law. To have deprived the secured creditors of the right to prove and obtain dividends on the full amount of their claim would have been a violation of the rights of the secured creditors and would have subjected the reorganization plan to proper criticism on their part.

5. *The approval of the plan of reorganization was a proper exercise of the discretion vested in the District Court.*

The fact that the great majority of creditors approved of the plan, does not establish the plan to be a fair and proper one. It is, however, most persuasive evidence of the fairness of that plan.

> *Jameson* v. *Guaranty Trust Co. of New York* (1927, C. C. A. 7th), 20 F. (2d) 808, 815;
> *P. R. Walsh Tie & Timber Co.* v. *Missouri Pac. Ry. Co.* (1922, C. C. A. 8th), 280 Fed. 38, 44.

A determination of the fairness of the reorganization plan must, to a considerable degree, rest in the discretion of the trial Court. A plan of reorganization necessarily represents the compromise of conflicting claims. The exact mathematical adjustment of those claims is not always possible. As was said by Judge MAYER in *Habirshaw Elec. Cable Co.* v. *Habirshaw Elec. Cable Co. Inc.* (1924, C. C. A. 2d), 296 Fed. 875, 879:

> "The court, of course, must decide whether or not the plan is fair and equitable before it orders the sale which is the step precedent to effectuating the plan. It is rare that such a plan is academically perfect. In the maze of rights, compromises become necessary, and failure to agree upon some reasonable plan necessarily leads to unfortunate results, involving loss to those concerned."

The Circuit Court of Appeals for the 8th Circuit, in *Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.*, 28 F. (2d) 177, stated in its opinion, at page 186:

> "The reorganization of an *insolvent* business involves considerations (practical and legal) not present in the reorganization of a solvent business. * * * The former are compelled by the inexorable logic of a hard situation; are designed to save as much as may be from impending wreckage and always involve changes in the existing legal rights of some (often all) of those having such rights in connection with the property involved." (Italics by Court.)

That Court had previously stated in its opinion, at page 184:

> "* * * In short, each *such reorganization must be examined and determined in a practical way* with a view of preserving the prior rights of unsecured creditors as far as may be having in mind the *necessities of the situation of the particular property.*"

That Court further said, in its opinion, at page 184:

> "* * * It is firmly established that *when a matter is committed to the sound discretion of a chancellor, his*

determination thereon will not be set aside unless clearly shown to be erroneous. The wisdom of this rule is accentuated where the matter involved is the reorganization of an insolvent property in receivership under the chancellor approving or disapproving the plan of reorganization. *The administration of an insolvent operating property during receivership is so largely a practical business matter that the chancellor gains an experience and insight into the property, its condition, its needs and the relative attitude of interested parties which can never, in its entirety, be transmitted to the printed record. From this intimate association with the property must necessarily come no inconsiderable portion of the 'informed discretion concerning the practical adjustment' of the chancellor."*

Judge KNOX, who approved of the reorganization plan, had appointed the Receiver herein. He was in charge of the administration of this and other receivership estates. He was familiar with the history of the receivership and the manner in which it had functioned. He had gained a familiarity with the nature of the property which affected his discretion in determining the proper method for its administration. In rejecting the plea of petitioners for an immediate liquidation, he said (R. 131):

> "The experience that I have had in seeing businesses such as this liquidated has been of a character as to lead me to believe that not much is to be hoped for from that standpoint; * * *."

Having due regard to "the necessities of the situation of the particular property" and the desires of the great majority of the creditor body, he properly approved this plan of reorganization which gives fair and practical recognition to the rights of *all* creditors. He found (R. 152):

> "8. Said offer is fair and equitable to all of the creditors of defendant and its acceptance upon the terms herein stated is in the best interests of such creditors."

That finding is clearly right.

SECOND POINT.

Assuming, however, that the District Court lacked the power to compel dissenting creditors to accept something other than cash in satisfaction of their claims, or that it improperly exercised its discretion in approving the plan of reorganization, the rights of petitioners received full and proper recognition in the decree of the Circuit Court of Appeals.

The Circuit Court of Appeals sustained petitioners' claim of a substantive right to be paid in cash. It decreed that a Special Master ascertain and award to petitioners their ratable share of the value of defendant's assets on public sale. Thus, it substituted for the ritual of public sale the appraisal of a Special Master. That Court also gave to petitioners the option of claiming the cash value of the notes and preferred stock offered to assenting creditors under the plan of reorganization, to be determined by a like appraisal.

1. *Petitioners were entitled to no more than their pro rata share of the distributable value of the defendant's assets and this was awarded to them by the Circuit Court of Appeals.*

The petitioners were entitled to neither a greater nor a lesser share than any other unsecured creditor. Had the defendant's assets been sold for cash, petitioners' rights would have been fully satisfied by a ratable share in the proceeds available for distribution after the payment of prior claims and proper administration expenses.

As was said in *Phipps* v. *Chicago R. I. & P. Ry. Co.* (284 Fed. 945, 949), upon the appointment of a receiver

> "that court held all that property in trust, subject to liens of the secured creditors, to operate it and to distribute it or its proceeds to all the unsecured creditors

and all the stockholders of the insolvent company according to the respective ranks and equities of their claims. *Every unsecured creditor then and thereafter was a cestui que trust of the court, entitled to a like interest in the property in proportion to the amount of his claim, as every other such creditor* and every stockholder was a cestui que trust of the court, entitled to a like interest in the property in proportion to the amount of his stock to that of every other stockholder. When that court had so operated the property, and by its decree had so distributed either the property itself or its proceeds, it had faithfully executed its trust and rendered the right decree."

Judge NOYES, of the Circuit Court of Appeals for the Second Circuit, dealing with the rules applicable to the administration of assets in an equity receivership, said in *Pennsylvania Steel Co.* v. *New York City Ry. Co.* (1918), 198 Fed. 721, at 738:

"Equitable considerations must govern and the underlying ones are these: The assets of an insolvent corporation belong to its creditors. Although not, strictly speaking, a trust fund, they partake of the nature of one. The administration of the estate is for their benefit. Its purpose is to make an *equitable distribution. Equality is equity.*"

The Circuit Court of Appeals gave petitioners their proper *pro rata* share of the defendant's assets. The decision of the Circuit Court provides (R. 173):

"* * * But the minority creditors, appellants, insisting upon the right to share immediately in the proceeds of a forced sale of the corporation's assets, have dissented. Their rights must be protected. They are ordinarily entitled to a public sale with competitive bidding, the assets to be sold to the highest bidder. They have a just claim to *their proportionate share of the price which would have been realized at such sale after deduction of administration expenses.*"

And, further (R. 174):

> "* * * This sum must be paid in cash, or, *at the option of each of the appellants, the preferred stock and notes offered to them may be valued as of the date the reorganization plan became effective, and that sum paid in cash to them or either of them.*"

The decision of the Circuit Court of Appeals grants to petitioners the option of claiming their *pro rata* interest in defendant's assets, either on the basis of forced liquidation or on the basis of a going concern. Petitioners have no equitable claim to more.

The Circuit Court of Appeals held that petitioners' proportionate share of the price which would have been realized at public sale was subject to "deduction of administration expenses" (R. 173). Petitioners object to the provision for administration expenses and protest against the payment of any part thereof.

It may fairly be assumed that the Circuit Court of Appeals intended the words "administration expenses" to mean proper expenses of administration. The District Court, in its order on the mandate of the Circuit Court of Appeals, has so construed these words. That order provides that the Special Master in ascertaining the amount to be awarded to petitioners shall take an account of "the expenses of the administration of the estate herein incurred up to the 15th day of June, 1931" (*vide*, Pets.' Br., p. 63). It further provides that the petitioners shall be charged with "such portion of the obligations of the receiver and the expenses of administration therein as would have been *properly* chargeable against the estate had the assets of Morris White, Inc. been liquidated by sale, * * *" (*vide*, Pets.' Br., p. 64).

The proper expenses of administration must, in every case, be paid. The decision of the Circuit Court says no more than that. If petitioners wish to object to the future allowance of any administration expenses upon the ground that such particular allowances would be improper, that question can

and should be properly raised at the time that the application for an allowance is made. It is not properly at issue here.

2. *The Court had power to dispense with an actual public sale of defendant's assets and to substitute therefor the appraisal by a Special Master.*

In an equity receivership, a public sale of the assets is part of the usual formula of administration. It is a procedural device for converting the assets into cash so that the proceeds may be distributed among creditors. It is, however, no more than a part of the machinery of administration which has for its purpose to effect the requisite equitable distribution of defendant's assets. It is part of the remedy but not of the right. The procedure which the Court may adopt for the liquidation of defendant's assets is a matter subject to the proper discretion of the Courts.

A public sale of the assets is not essential to the proper administration or distribution of the estate. In *Phipps* v. *Chicago R. I. & P. Ry. Co.*, 284 Fed. 945, Judge SANBORN stated in his opinion, at page 949:

> "* * * The decisions in those cases [the *Boyd* and *Kansas City Southern* cases] demonstrate the fact that judicial sales are futile to extract the vice of a failure by a plan of reorganization and decree to secure to creditors their equitable shares of the beneficial interests in the reorganized corporations, and that fact is in itself a persuasive argument that a *plan of reorganization and decree which does adjudge and secure or offer to the creditors their just and fair shares of the benefits of the reorganized company,* either in its stocks, bonds, or other securities, *is just, fair, and imperrious to the attacks of such creditors, although no judicial sale is adjudged thereby or made thereunder.*"

In his opinion, at page 952, Judge SANBORN, referring to the case of *St. Louis-San Francisco Ry. Co.* v. *McElvain,* 253 Fed. 123, said:

> "It is true that there was a judicial sale in that case, and that in the case in hand there has been no judicial sale; but it was not the judicial sale that made the decree and the title of the reorganized company in that case impervious to the attacks of the creditors of the old company. It was the offer to them in stock of the reorganized company of *their fair and equitable shares in the benefits* of the participation in that company. *A like decree without the sale would have been equally conclusive.*"

That there is no vested right to any particular form of remedy or any particular mode of procedure is firmly settled law.

> *National Surety Co.* v. *Architectural Decorating Co.* (1912), 226 U. S. 276;
> *Pittsburgh Steel Co.* v. *Baltimore Equitable Soc.* (1913), 226 U. S. 455;
> *Wilson* v. *Standefer* (1902), 184 U. S. 399;
> *Penniman's Case* (1881), 103 U. S. 714.

A Court of equity has power to modify its procedure and to mold its remedies in giving effect to substantive rights. This is established beyond question. In *Union Pacific R. Co.* v. *Chicago, R. I. & P. R. Co.* (1896), 163 U. S. 564, this Court stated, at pages 600-601:

> "*It must not be forgotten that in the increasing complexities of modern business relations, equitable remedies have necessarily and steadily been expanded, and no inflexible rule has been permitted to circumscribe them.* As has been well said, equity has contrived its remedies 'so that they shall correspond both to the primary right of the injured party, and to the wrong by which that right has been violated;' and 'has always preserved the elements of flexibility and expansiveness, so that new ones may be invented, or old ones modified, in order to meet the requirements of every case, and to satisfy the needs of a progressive social condition in which new primary rights and duties are constantly arising and new

kinds of wrongs are constantly committed.' Pom. Eq. Jur. Sec. 111."

In *Graselli Chemical Co.* v. *Aetna Explosives Co.* (1918, C. C. A. 2d), 252 Fed. 456, 459, the Court said:

> *"A court of equity's modes of relief are not fixed and rigid. It can mold its remedies to meet the conditions with which it has to deal.* The jurisdiction of equity is the whole domain of conscience, limited only by legislative enactment. The faculty of equity must be energetic, productive, and progressive."

The Court further stated (p. 460):

> "* * * In the absence of power created by legislation in this country, the federal judges, sitting in courts of equity, have endeavored to secure to the rights of those interested, including the stockholders at the time of readjustment of large corporations a protection to meet the needs of the occasion. *Changing times, with change in economic needs, require the courts of equity to mold remedies to meet the conditions with which they have to deal."*

The *Aetna Explosives* case, *supra,* is not overruled in *Manhattan Rubber Mfg. Co.* v. *Lucey Mfg. Co.* (1925, C. C. A. 2d), 5 F. (2d) 39, as petitioners' brief (p. 29) implies. It is cited with approval in the prevailing opinion of Judge Manton (pp. 40-41) and in the dissenting opinion of Judge Hough. In such opinion, Judge Hough stated, at page 43:

> "* * * Thus the primitive view of a bill like this one led to regarding it as no more than the reduction to the court's possession of a certain amount of property and to confining the activities of chancery to the preservation, distribution, or restoration of that property to or among the persons entitled to the same.
>
> *But no one was ever able to know beforehand the ramifications of such a matter, or to foresee the demands that would be made upon the discretion, the boldness, or the inventive ability of the court whose aid creditors, shareholders, and directors united in seeking.* * * * *Such conditions, political and commercial, are increasingly*

presenting new and vexatious questions loudly calling for what one of our ablest judges has called 'the plastic remedies of equity.'

Such a situation was acutely presented to this court in *Graselli, etc. Co.* v. *Aetna, etc. Co.*, 252 F. 456, 164 C. C. A. 380. * * * It [the decision in the *Aetna Explosives case*] was made after exhaustive argument by counsel of learning, *and the result was of primary importance if equitable proceedings for reorganizations or in insolvency are to continue and to grow, as all living things must grow.*"

A court of equity will vary its usual methods of relief according to the exigencies of the case. The usual rule in foreclosure proceedings is that the rights of all parties claiming an interest in the property shall be adjudicated in advance of the sale. That this rule of procedure is subject to change in the proper discretion of the Court, was decided in *First National Bank of Cleveland* v. *Shedd* (1887), 121 U. S. 74. In that case, proceedings for the foreclosure of two trust mortgages were pending. A dispute arose as to the extent of the priority of the first mortgage and as to the amount due thereunder. The District Court ordered a sale of the properties in advance of the determination of these questions. In its opinion, the Court, speaking by the Chief Justice (WAITE) said, at page 87:

"* * * *The court below, having the practical workings of the receivership under its own eye,* did not hesitate to say that 'it is now entirely clear that the best interests of all parties concerned will be promoted by a speedy sale,' and we see nothing to the contrary.

Of the power of the court to make such an order in a proper case we have no doubt. *The property is in the possession of the court and is depreciating in value by the accumulation of receiver's indebtedness, while the litigation between the parties as to their respective interests in it is going on.* There cannot be a doubt that the whole ought to be sold together. If in the end it shall be found that the Rawle mortgage covers only a part, it will be as easy to fix the rule for dividing the proceeds equitably

between the two securities after a sale, as before, and there is nothing in the decree as entered to interfere in any way with such a distribution."

3. *Appraisal by a Special Master in lieu of public sale was a proper method of determining the value of petitioners' interests.*

The determination of value by appraisal, in lieu of public sale, is not only practical but common. Indeed, the Solicitor General in his report dated December 8, 1931, to which we have already referred (*supra*, pp. 35, 36), recommended (p. 90) that the Bankruptcy Act be amended to permit reorganizations approved by the majority of the creditor body and suggested that the interests of dissenting creditors be fixed by *appraisal*, and liquidated by cash payment. His suggestion (in subdivision (f), (5) (c) of the proposed new Section 76 of the Bankruptcy Act) is that the claims of dissentients may be satisfied, *inter alia*, "by appraisal and payment in cash of the value of such liens and claims, or, at the objecting creditors' election, of the securities allotted to such liens and claims under the plan". (Appendix to Solicitor General's Report, p. 92). The Court will note that the Circuit Court of Appeals gave petitioners precisely what the Solicitor General suggests as the proper measure of relief to dissenting creditors.

Appraisal is a method which long has been used to fix the cash value of the interest of minority stockholders who oppose a sale of corporate assets or corporate mergers. (Lattin, *Remedies of Dissenting Stockholders under Appraisal Statutes* (1931), 45 Harv. L. Rev. 233; Weiner, *Payment of Dissenting Stockholders* (1927), 27 Col. L. Rev. 547).

Stripped of outward forms and regarded as a matter of substance, Federal Courts have, under the guise of an "upset price", fixed the value of assets sold in an equity receivership and have thereby determined by appraisal the *pro rata* cash payment to be made to dissenting creditors. In theory the upset price represents the minimum bid which the

Court will accept for the assets. In practice it represents the maximum price which will be paid for those assets. (Weiner, *Conflicting Functions of the Upset Price in a Corporate Reorganization* (1927), 27 Col. L. Rev. 132, 138). In receiverships of large corporations, there are rarely any bidders for the assets other than the reorganization committee. (Weiner, *id.*, p. 138). The upset price is intended to protect the interests of the dissenting minority. (*Investment Registry* v. *Chicago & M. E. R. Co.*, (1913, C. C. A. 7th), 212 Fed. 594, 609, 610). The upset price is, thus, a determination by the Court of the cash payment to be awarded to dissenting creditors. In directing that the value of the defendant's assets on public sale be determined by the appraisal of a Special Master instead of by an actual sale, the Circuit Court in this case did no more than what Courts of equity have repeatedly done under the guise of fixing an "upset price." It merely dispensed with what had become an empty form.

Petitioners argue that the decision of the Circuit Court of Appeals is "too indefinite and is impossible of performance". Petitioners' argument assumes that it is not possible for the Special Master to ascertain what assets were transferred or to determine "the value of the assets as if sold at a public sale" on June 15, 1931. In both assumptions, petitioners err.

A determination by the Special Master of the assets transferred pursuant to the decree of the District Court, presents no unique or extraordinary problem. The same problem would have been presented if the Circuit Court of Appeals had reversed the decree of the District Court in its entirety and had required the reorganized corporation to account for the assets which it had received. Such a problem has heretofore arisen on the *vacatur* of a bankruptcy sale, and the judicial machinery of an accounting before a Special Master has been found adequate therefor. *In re Prudential Outfitting Co.* (1918), 250 Fed. 504, 507.

A determination of the value of the assets as if sold at a public sale, on June 15, 1931, a date antecedent to the Special Master's determination, presents a simple question of fact.

Similar questions are regularly presented for judicial determination. Upon an application to vacate a sale in bankruptcy upon the ground of inadequacy of consideration, the court must determine the value of the assets at the date of sale. Under statutory provisions, which exist in practically every state, stockholders who oppose a sale of the assets of the corporation may, subsequent to the date of sale, obtain an appraisal of the value of their interest in the assets of the corporation at the date of the sale, and claim that amount in cash (*Jackson Co.* v. *Gardiner Inv. Co.* (1914, C. C. A. 1st), 217 Fed. 350). In the ordinary action for breach of contract of sale, the Court must often determine the market value of goods as of a date several years prior to such determination. In *Southern Pacific Co.* v. *Bogert* (1919), 250 U. S. 483, 496, this Court remanded the case to the trial court for the purpose of determining far more complicated questions of fact which had arisen in connection with a reorganization over thirty years prior thereto.

A determination of the questions presented to the Special Master under the order of the Circuit Court of Appeals is clearly within the scope of ordinary legal procedure.

Petitioners complain that they are not adequately protected by the decree of the Circuit Court of Appeals. That decree provides "If payment is not thus made in cash, the several amounts which appellants are found entitled to may be collected by a sale of the property transferred to the new corporation" (R. 174). The decree of the District Court entered upon the mandate of the Circuit Court of Appeals awards petitioners a lien on all the assets of Morris White, Inc. in the posssession of the reorganized corporation and enjoins the reorganized corporation from transferring any of said assets "except in good faith in the regular course of its business and for fair and proper consideration " (*Vide* Pets.' Br., p. 67). Petitioners' claims if proved and allowed represent approximately 10% of the defendant's liabilities. The Circuit Court of Appeals awarded to the claims of petitioners a priority over the interests of the assenting creditor body

and the District Court, by its order, has enforced that priority. Indeed, the District Court enjoined the reorganized corporation from making payment to the assenting creditors upon the notes due on January 2, 1932, and directed that the sum of $33,000 deposited by the reorganized corporation for that purpose be held pending the further order of the Court (Pets.' Br., p. 67). The decision of the Circuit Court and the decree entered by the District Court, pursuant to the mandate of the Circuit Court, afforded to petitioners an abundant protection.

4. *The situation presented to the Circuit Court of Appeals required that Court, in the proper exercise of its discretion, to direct the appraisal instead of a public sale.*

The discretion of a court of equity in awarding any particular method of relief is governed by the particular situation which confronts it at the time of its decision. The decision of the Circuit Court of Appeals was handed down on November 16, 1931 (R. 164). The assets had then been transferred to the purchaser pursant to the decree of the District Court on June 15, 1931 (R. 173). The plan of reorganization had become operative (R. 173). The vast majority of the creditor body desired the reorganization to continue in effect (R. 173). The purchaser had continued the operation of the business. Actual sale as of June 15, 1931 was obviously impossible on November 16, 1931. Only an estimate was possible.

Substantial damage was certain to result from a decree that the sale be set aside in its entirety and that the assets be sold at public sale. Delay would have necessarily occurred between the time of such decree and a public sale held pursuant thereto. Prior to such sale it would have been necessary for the purchaser to render its accounting for the assets which it had received and much time would have been consumed therein. Sufficient advertisement of sale meant further delay. In the meanwhile, the business of the reorgan-

ized corporation would have ceased to function and the industry in which it occupied a dominant role, would have come to a standstill (R. 103). The trend of prices was downward (R. 126-7) and the value of the inventory was bound to depreciate. A further impairment of the good will of the business was certain to result from a cessation of operations. The expense of the preservation of the assets, pending resale thereof, would have placed an additional burden on the estate.

The benefits to be gained from an actual sale were dubious. The costs and charges incident to such a sale were substantial (R. 131). Whether any cash bid, worthy of the Court's consideration, would have materialized was uncertain. On this point, the proceedings had in the District Court were significant. In accordance with the order of the District Court, the Receiver published notice in the New York Times that a hearing would be held to consider all offers for the purchase of the defendant's assets (R. 16). Several prospective purchasers made inquiries, but upon the hearing there were no bids, and the District Court found as a fact (R. 151):

> "3. No offer other than said offer of Lily White dated April 29th, 1931 for the purchase of the assets of the defendant and of the Receiver's right, title and interest therein has been made."

The absence of bidders may be explained by the fact that the assets of the estate were subject to prior liens for unpaid taxes due to the Federal and State Governments for which, claims in excess of $150,000 had been filed. Unless the cash bid were in an amount sufficient to discharge the tax claims and proper expenses of administration, which were entitled to priority, nothing would be realized by unsecured creditors. The likelihood of obtaining a cash bid of at least $150,000 on public sale during the current depression is, to say the least, highly speculative. Appraisal by the Special Master was far more likely to approximate the true liquidation value of defendant's assets.

In rendering its decree and devising its remedy, the Circuit Court of Appeals properly gave consideration, not merely to the rights of petitioners, but to the rights of all interested parties. In its opinion the Court said (R. 173):

> "*An outstanding circumstance is the willingness of the majority of creditors to proceed with this reorganization, expressing the view, as they did in the court below, that the rehabilitation of White's business gave the best promise for the payment of their debts.* * * * But the minority creditors, appellants, insisting upon the right to share immediately in the proceeds of a forced sale of the corporation's assets, have dissented. Their rights must be protected. * * * *If a court of equity can protect these rights and at the same time carry out the wish of the other creditors who favor the plan of reorganization, it should be done.* The reorganization plan has been put into operation, and creditors, excepting the appellants, are content to have it proceed. *We think both may be protected.*"

The ritual of public sale would have added nothing to petitioners' substantive rights. On the contrary, it meant disruption of the reorganized business and loss to the estate. In substituting the determination of the Special Master, the Circuit Court merely dispensed with an empty and burdensome formula of adjustment and provided in its stead a remedy in accordance with the existing situation and the true balance of convenience. If, therefore, the Circuit Court of Appeals was correct in its determination that the dissenting creditors must be paid in cash, the procedure devised by that Court marks "a desirable development in the law of corporate reorganization." (*Coriell* v. *Morris White, Inc.: A Recent Development in the Law of Corporate Reorganizations*—(1932) 45 Harvard L. Rev. 697, 699.)

CONCLUSION.

The decree of the District Court, dated June 15, 1931, was a proper exercise of the power and discretion of that Court. It did not violate the petitioners' rights in requiring petitioners to accept something other than cash in satisfaction of their claims. Petitioners have no claim to any greater rights than were awarded to them under that decree. If, however, the District Court was in error, petitioners' claims have received proper and adequate recognition under the decree of the Circuit Court of Appeals.

Respondents therefore pray that the decree of the Circuit Court of Appeals be affirmed.

Dated: New York, December 7, 1932.

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